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# Senator Dianne Feinstein

of California

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## **Senator Feinstein Invites Governor Schwarzenegger to Work on a New Energy Framework to Avoid Looming Power Outages**

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**Washington, DC** – Concerned about looming blackouts, Senator Feinstein has written to California Governor Arnold Schwarzenegger and invited him to work with her to establish a new energy framework for the State of California. Based on current estimates, the State could face blackouts or energy shortages in the next few months to three years.

Senator Feinstein supports a framework that would promote timely and adequate investments in efficient, cost-effective, environmentally-sustainable resources and ensure customers reliable electric service at reasonable cost. The central element of the framework that Senator Feinstein has proposed calls for:

- The development of a cost-of-service based system (cost, plus a reasonable profit) for service to those 70% of Californians who get their power from investor-owned utilities. These rates would be regulated by the California Public Utilities Commission.

At the same time, very large consumers -- those companies that use 500 KW and above (mainly industrial, agricultural, and manufacturing operations) -- would have the option to choose between this regulated system and the open market. Large consumers would be bound to the choice they make for a specific amount of time (such as five years) and would be responsible for their share of costs for system improvements and system reliability.

*The following is the text of Senator Feinstein's letter:*

"I am writing to express my concern that California could, in the next few months to three years, experience another energy crisis and to invite you to work with me on a framework that would allow the State to avoid such an outcome. It is my strong view that the State is in jeopardy because of a lack of sufficient investment in electricity infrastructure and because deregulation has not worked. At a minimum, we need to turn to a system where a vast majority of consumers are protected under a cost-of-service based system.

The California Independent System Operator warns that an adverse combination of events (specifically reduced hydroelectric production, low wind production, a hot summer, and high demand) could cause electricity shortages by summer 2004. Under such circumstances, the demand is expected to be 46,573 MW, while the supply could be as low as 45,000 MW (one megawatt provides enough power for approximately 750 homes). By 2006, the numbers are

more daunting. The California Independent System Operator projects that demand could reach 48,337 MW while supply could be as low as 46,002 MW.

In addition, the California Energy Commission warns that the reliability of the electricity grid could be in jeopardy by 2006 if more generating capacity is not brought online. Yet much of the new generation approved in the wake of the energy crisis is not online—only 2,165 MW of the 7,852 MW approved, but not yet built, are currently under construction and on schedule.

Further, over 20,000 MW of existing generating capacity have been sold pursuant to orders of the California Public Utility Commission under California's deregulation plan and are now owned by unregulated, independent power producers. These generating facilities are, for the most part, over 35 years old, largely inefficient, and costly to maintain. Reliant Energy, as one case in point, has decided to mothball three inefficient generators totaling 824 MW. The California Independent System Operator estimates that an additional 3,800 MW of existing generating capacity are at risk of being taken offline in the next five years and that an additional 3,870 MW are similarly at risk of being retired in the next several years. In sum, California is at risk of losing over 7,500 MW of power over the next several years—power for approximately 5.7 million homes.

Simply put, the problem in California today is that sufficient new generation is not being built to keep up with rising electricity demand, while at the same time older, less efficient plants, are being retired. The key is that there must be sufficient new investment to ensure that utilities can continue to provide reliable, reasonably priced electric service. However, new investment is contingent upon the development of a certain, stable framework that will allow the utilities to provide the initial capital investments subject to the recovery of, and a reasonable return on, those investments over the estimated useful life of the facility through just and reasonable rates approved and maintained by the Commission.

Since I know that you share my concern for California's energy future, I would like to suggest a framework for your consideration that would promote timely and adequate investments in efficient, cost-effective, environmentally-sustainable resources and ensure customers reliable electric service at reasonable cost.

The basis for this framework is to ensure reliability and reasonable prices for consumers. In other words, consumers should be protected from price spikes, market manipulation, and blackouts. Clearly, for consumers, the 1996 deregulation was a failure in California.

Approximately 70% of all Californians are served by the investor-owned utilities. The key elements of the framework I propose mainly deal with this 70% of consumers and include the following:

- Development of a cost-of-service based system for those 70% of Californians served by the investor-owned utilities. The cost-of-service based rates would be regulated by the California Public Utilities Commission. At the same time, very large consumers (500 KW and above) would have the option to choose between this regulated system and the open market. Large consumers would be bound to the choice they make for a specific amount of time (such as five years) and would be responsible for their share of costs for system improvements and system reliability.

- Legislatively reinforce that investor-owned utilities have a mandatory obligation to serve their customers. This obligation includes the obligation to plan and invest in or contract for needed resources, and would mandate that the utilities must meet 100% of their customers' annual highest demand. In order to meet that demand, the utilities must have enough power on reserve to meet unexpected outages. This reserve margin would increase by 2% per year beginning in 2005 until a minimum 15% reserve margin is met. Fifteen percent is the well-established reserve margin above expected peak demand to ensure that California consumers never again face electricity shortages. This reserve margin would help to prevent price spikes or price manipulation by ensuring that the utilities have enough power on hand to meet their customers' needs in case of unexpected outages or high temperatures. Utilities would be able to make adequate investments in needed resources because they would know exactly who their customers are for an extended period of time. These same requirements would apply equally to any other entity providing electric service to customers.
- Require the utilities to develop an integrated resource investment plan that includes: demand/supply forecasts for 5-, 10-, and 15-year periods; energy conservation and energy efficiency measures; and, an assurance that adequate resources are available to reliably serve customers. Further, the plan should require utilities to promote the use of ultra-clean distributed generation so that smaller, clean generators can be used by apartment buildings, businesses, or small communities as long as those generators do not add to the state's air quality problems. The plan will be subject to review and approval of the California Public Utilities Commission.
- Mandate investments in new or expanded transmission facilities to ensure efficient use and reliable operation of the grid. The customers exempted from cost-of-service rates (above 500 KW) would also pay their fair share.
- Require investments in the electric distribution grid to ensure the continued safe, reliable, efficient, and cost-effective operation of the distribution grid. Large customers (above 500 KW) would continue to pay an appropriate share of the costs to improve the distribution grid.

As part of meeting the obligation to serve, utilities should be required to make investments which will improve system reliability, increase fuel diversity, and lower costs to consumers including energy efficiency and demand-side reduction technologies, renewable generation, repowered generation, high efficiency cogeneration and ultra-clean distributed generation. Specifically, these investments would include:

- Energy Efficiency and Demand Response: Energy efficiency investments help improve system reliability by reducing consumption, especially at times of high demand. Every kilowatt hour saved is one that does not have to be produced and will result in fewer air emissions and less fuel consumption statewide. Utilities should first invest in cost-effective energy conservation technologies.
- Renewables: Renewable energy helps to diversify our energy resource portfolio, thereby protecting California consumers from natural gas price volatility. The current renewable portfolio standard requires that California utilities purchase renewable energy such as

geothermal, wind, solar, and biomass under long-term contracts at or below a market price established by the Commission. Utilities are now required to have 20% of their generating capacity come from renewable resources by 2017. Utilities should increase their investments in renewable generation in order to meet the renewable portfolio standard of 20% renewable generation by December 31, 2010.

- Repowered Generation and High-Efficiency Cogeneration: California has over 20,000 MW of existing generating capacity that is old, inefficient, and nearing the end of its useful life. Many of these plants are located close to high demand areas, and already have existing infrastructure (such as transmission and gas supply). To maintain system reliability, improve efficiency, and lower costs to consumers, many of these plants should be upgraded to meet current standards. Cogeneration operates at higher efficiency and produces fewer emissions than traditional gas plants. High-efficiency cogeneration also directly supports some of California's most important industrial and commercial jobs and products. Utilities should invest in repowering and high-efficiency cogeneration projects that offer equivalent or better system reliability, equivalent or better environmental benefits, and equivalent or lower costs to ratepayers than new generation.

I would be pleased to meet with you at your convenience to begin the necessary work to ensure that our State will be able to face its energy challenges. Since investments in efficient, cost-effective supply and demand resources cannot be made overnight, it is imperative that the State of California puts in place a secure framework as soon as possible. I look forward to working with you in this important endeavor.”

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